# DOW THEORY LETTERS INC.

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THE MARKET: I urge subscribers to study the following discussion of the price movement carefully. The whole Rail-Industrial relationship may now be telling an important story. In October (see Chart 1) the two Averages recorded their last confirmed highs. Thus, the primary trend was recently reconfirmed as bullish, and from the standpoint of Dow's Theory it will remain bullish until proved otherwise. Following the October high, Rails immediately went into a reactionary phase while Industrials continued higher, the latter recording a new all-time high in November.

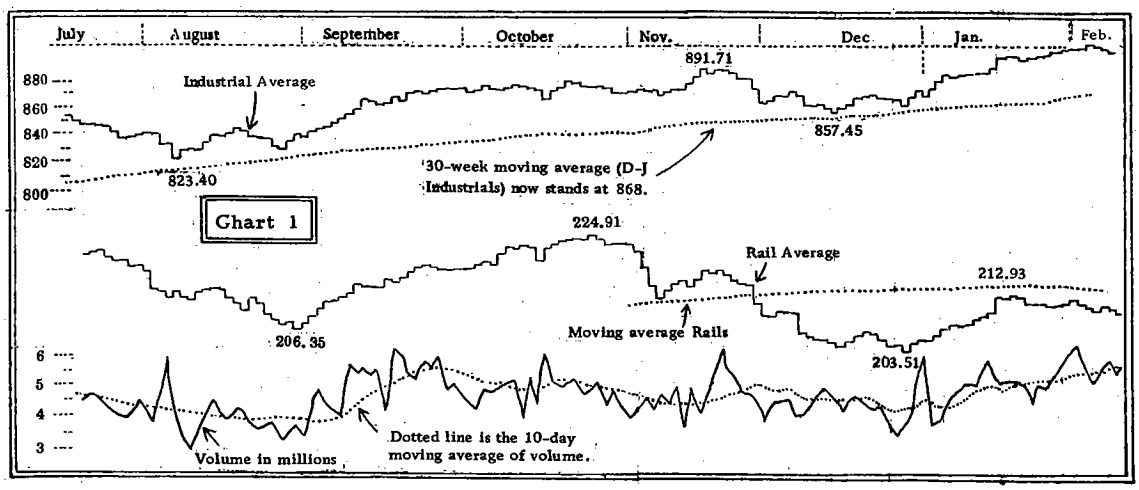
The persistent retreat of the Rails turned the Industrials down in December, however. On December 15 the two Averages established lows. A little rally followed, but Rails declined again. On December 30 the carriers broke to a new low of 203.51 (actually below their August low). Industrials refused to confirm. The non-confirmation by Industrials set the stage for the December-January rally.

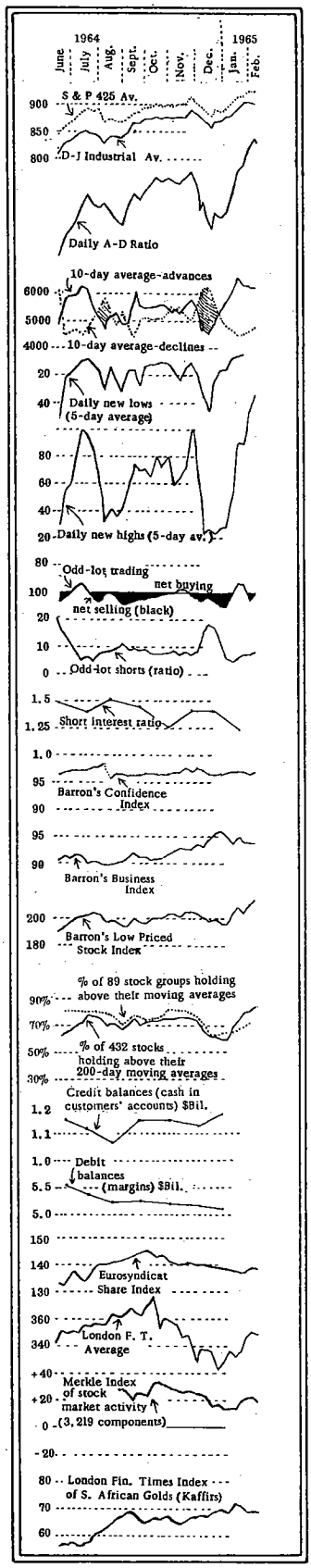
In the last Letter I drew attention to the non-confirmatory action of the Rail Average, and I stated that although confirmation is not an immediate necessity, the health of the market nevertheless requires that the two Averages advance together. This has not been the case since mid-January (see chart). By early February, in fact, while Industrials continued into all-time high territory, the Rails traced out a definite downward zig-zag. This action assumed a particular interest in view of the extremely heavy volume which accompanied the divergence. The great Dow Theorist Robert Rhea observed that when the Averages "disagree" and when volume is running high, the market is saying "be careful."

On February 8, in supposed response to a weekend flare-up in the Viet Nam war, the Averages retreated again on high volume, and a second downward zig-zag was thereby formed in the Rail Average (which is rather unusual in view of the fact that Rails usually rally on "war news" and are considered to be "war babies"). It is notable that the Rails have not only refused to confirm in a primary sense (by bettering their former high of 224.91), but they have even refused to confirm in a secondary sense by bettering their recent January high of 212.93.

Conclusion: The primary trend is bullish. The secondary trend is obscure but will be bullish if Rails move up (with Industrials) above the 212.93 level. Subscribers should remember that the last secondary low points were recorded in December at 857.45 and 203.51. Those levels will continue to represent the bear points until (or unless) Rails better their high of 224.91. Stated another way, it is only when the two Averages rise to new bull market highs that the significance of all previous levels is erased.

Question: If the two Averages were to turn down (prior to a new Rail high) and break their December lows on high volume, I realize that you would then say that the primary trend had turned bearish. If this were to occur, where would the bull market top have been? Answer: History would then record



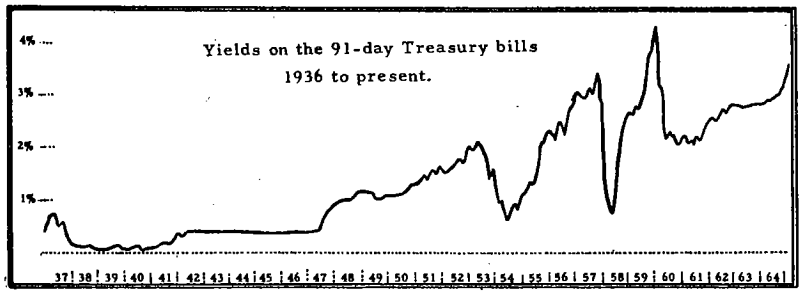



October 20 as the bull market high; that was the day when the two Averages recorded their last confirmed highs.

The Composite Chart on Page 1 shows the two Industrial Averages declining somewhat while the A-D ratio (on Monday, February 8) corrects after outperforming the Averages for two weeks. The superior performance of breadth is reflected in the new highs which last week rose to their highest (5-day average) since last April and in the percentage of stocks holding above their moving averages which is now 84%. The 10-day averages of advances (and declines) continue to show the market as overbought. Odd-lotters are still selling but less so than during the fourth quarter of last year. The Confidence Index is still stringing out sideways, while last week saw the low-priced stock index at a new 1964-65 high of 214. The London market has fully corrected its recent decline, while the Eurosyndicat Index continues to reflect the generally desultory action of leading European shares. The Kaffirs (gold) index has held near its 1964-65 high despite (as James Dines puts it) "the strongest anti-propaganda blast since before Roosevelt devalued the dollar."

Conclusion: Except for debits, the Confidence Index, the Rail Average, and perhaps the short interest ratio (in view of the recent heavy volume), the indicators shown here reflect general strength rather than weakness.

MONEY: Last week the yield on the U.S. Treasury's 13-week (or 91-day) bill rose to 3.90%, highest level in five years (see chart). I have received an increasing number of inquiries about Treasury debt, and this appears to be a good time to discuss it in further detail (see Letter 274 on bills).




The Treasury issues four classifications of debt, each based on length of maturity and method of interest payment. At the short end, the bill represents a debt instrument of one year or less. Bills are issued in denominations of $1000 and are sold on a discounted basis. This means that interest is subtracted from the purchase price at the time of purchase. For example, you might now pay $4940 for $5000 of 91-day bills maturing in May. Bills are sold by the Treasury at auction which takes place weekly, and bills are always quoted on a yield basis. Bills may be conveniently purchased through your broker or bank. There is an insignificant charge or commission of less than $1 per bill.

Certificates are issued for one year's maturity or less but they are not sold on a discounted basis. Certificates are issued at par with coupons attached (coupons are turned in for interest at maturity). Notes are issued for maturities of one year to less than five years. Notes carry coupons and are issued in denominations of $100 or $1000 or more. Finally, bonds are issued in denominations as low as $500, and they are always in maturities of five years or more. All of these debt instruments, bills, certificates, notes and bonds are negotiable and may fluctuate in price on the open market. The single exception is the savings bond, which the purchaser may sell at any time at a fixed price-scale (selling price depends upon length of time held) or at maturity.

All of these debt instruments represent a definite legal call on the full assets and taxing power of the Unites States Government. They must be paid in full as they fall due — otherwise, the Government is in the position of declaring itself bankrupt. The most liquid and least risky (in terms of smallest fluctuations) of the Treasury debt are the bills. The Government must redeem these at face value within a year. For all purposes, bills are tantamount to cash.

At their current fat yield of 3.9% I recommend 91-day Treasury bills as a repository for both personal and corporate cash. From a higher yield standpoint personal accounts may be placed in savings banks at rates up to 4.4% in New York. Many states do not have savings banks, but all states have commercial banks with savings departments, and here one may now obtain 4% interest, highest commercial bank interest in a generation. Corporations are not allowed to place money in savings banks or savings departments of commercial banks, and they must therefore choose Treasury bills or savings & loan companies. I prefer the former, since it represents debt of the U. S. Government while the latter represent "shares" (not debt but participating ownership) in a savings & loan institution.

Many corporations and individuals place funds in certificates of deposit. These are sums placed with a bank for a specified period of time. Certificates of deposit usually pay a higher rate of interest than that paid to a regular bank depositor. However, here the institution must be checked with care, since (from latest information) neither the Federal Deposit Insurance Corporation nor the Savings & Loan Insurance Corp. considers the certificate of deposit as anything more than a straight loan to the institution. As such, they do not insure these certificates. This fact is being learned the hard way by holders of certificates at the ill-fated San Francisco National Bank (which was just declared insolvent). Of the roughly $40 million deposited with this bank, almost half was in the form of certificates of deposit, and this money may be lost. Furthermore, regular depositors will probably lose all money in individual accounts above the specified limit of $10 thousand which is insured. Thus of almost $40 million deposited with the bank, perhaps $8 million will be paid off by the F.D.I.C. Moral: If you place your money with a bank or any other institution, make sure that the institution is conservative and solvent. Do not place more than $10 thousand in a single account in any single insured institution.

Conclusion: The safest place to put funds (assuming one wishes almost full liquidity) is in Treasury bills. Moreover, adding to the attractiveness of the bills is the fact that they are now near their highest yield in bill history. The accompanying chart traces the yield on 91-day bills from their inception in 1936 to the present. The chart shows what I take to be a bull market in yields and a bear market in U.S. Treasury debt. All of which brings back the words of Charles Dow penned in 1902: "After dear money has once come, it usually recurs, until it has its effect. The effect is always the same in the end. It means contraction, curtailment and lessened demand for funds. The more money has been tied up, the longer it takes to secure adequate liquidation. The sounder the situation, the less the unfavorable effect, but permanent relief from money absorbtion must come fhrough lessened demand." I leave it to subscribers; study the chart of the Treasury bill yields and draw your own conclusion as to possible coming events in the money market.

CASH (CREDIT) BALANCES: The following is from a letter received from famed bank credit analyst A. Hamilton Bolton (February 2). The letter refers to the credit-debit study in my Letter 278, and I thought it interesting enough to bring to the attention of subscribers. "In reading your letter this week concerning the unorthodox behaviour of free credit balances, I wonder, and have suggested to Dr. Sloan Wilson that it may be due to the monetary phenomenon which is behind the sky-rocketing (relative) in turnover of demand deposits, i.e. the shift to time deposits with high interest rates. Up to a year or so ago, it was not possible to get too good a return from deposits, consequently our stock market public would leave its money on deposit with his broker. Everybody now seems to be return conscious. One might therefore theorize that credit balances would have climbed much higher, in say the 1962-64 period than they actually did, and hence the decline since early 1964 was a lot less than it would have been. Of course, nobody can prove it."

THE STRUGGLE: Subscribers have displayed an extraordinary interest in the discussions which have appeared here regarding gold, Franco-U.S. power struggle and the whole subject of international politico-economics. One subscriber writes: "Your interpretations are different from almost everything else I read, they make sense, and they're of utmost importance. Please don't stop." So here goes:

DeGaulle is deadly serious about two possibilities: (1) France as leader of a new European "third force," (2) France as leader of the entire Free World. Although the first was openly ridiculed as late as a year ago, it is now widely recognized as not only a possibility but a probability. The second alternative, however, is considered to be out of the question. "It's absurd," people retort when the second possibility is mentioned, "why France is a second rate nation compared to the U.S. We have the power, the know-how, the productive ability, the population."

The answer to this as DeGaulle sees it is as follows: a European third force is now within reach. But France as leader of the West — that could only happen if the "Anglo-Saxon" nations, Britain and the U.S., suffered an economic collapse while France and Europe stood intact.

DeGaulle sees two avenues by which leadership of the West might fall to France. (1) Political. The French foreign minister, Couve de Murville, is coming to Washington on February 17 for an indefinite stay. Evidently, he is going to attempt some sort of meeting of the minds. But one thing is increasingly obvious. DeGaulle wants the U.S. out of Europe, "lock, stock and barrel." If DeGaulle can succeed in this, Germany with her economic power and large gold and dollar holdings (she is the largest holder of dollars in Europe) will fall into the French camp. Why? The answer is Germany's deep-seated fear of Russia. If De Gaulle can convince Germany that the U.S. is thinking of pulling out of Europe or that the U.S. will not back Europe in case of trouble, then he will have scored a stunning coup. For in the end, Germany can be counted upon to follow her own interests, and if she believes an alignment with France will serve her better than one with the U.S., she could well make the switch.

(2) Economic. But what would possibly make the U.S. get out of Europe? In a word, fear of a collapse of the dollar. Over the past few weeks, the U.S. has lost $300 million in gold. The situation is becoming grim and the Administration knows it. Already, it is rumoured that the U.S. is mulling over a "get tough" policy for the dollar and the economy. Last week Chairman of the Reserve Board Martin announced: "The continuing chronic deficits have put the U.S. behind the eight ball and we're playing for keeps when it comes to conserving our gold." Then, lo and behold, the following classic "about face" was described in the February 4 Wall Street Journal: "...Administration officials are coming to the view that if the Federal Reserve Board wants credit tightened 'somewhat' it should go ahead and do it." In other words, we don't want deflation, but if the Reserve Board wants to do something about the deficits, well, O.K., but you boys take the blame for the tight money too. And all last week (in preparation for coming events) the Treasury bond list sold off.

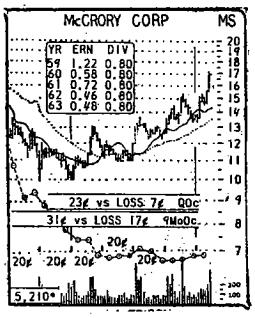
So with interest rates already high (see bill chart in this Letter), the U.S. now braces itself for the announcement that interest rates may go even higher. And for the first time in a generation, "hard money" nations from Europe are forcing "unpleasant" decisions upon an inflation-oriented U.S. Administration. This writer can almost hear the French Foreign Minister saying: "Ah my American friends, you simply must get your troops out of Europe. For this alone could do a great deal, perhaps even solve your chronic balance-of-payments defficulties. Europe can take care of itself, you take care of your weakening dollars."

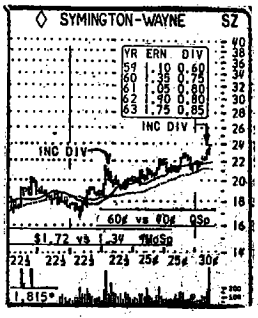
Late last week in one of his rare (and always widely publicized) press conferences DeGaulle spoke about gold and the dollar. His conference came at the most embarrassing possible time for the U.S. (as we were preparing to remove our 25% gold clause). France, DeGaulle said, believes that the pound and the dollar should be scrapped as reserve currencies. Gold should again be used as the sole vehicle for settlement of international accounts. Today, DeGaulle went on, the six Common Market countries hold as much gold as the U.S. If the six commong market countries were to convert their gold, into dollars (the threat), then they would have much more gold than the U.S. The dollar, he continued, has lost its "transcendent" value; the U.S. has tarnished its image of the dollar in that it shows itself willing to "settle its debts with dollars that it only has to print" instead of with gold "which has real value."

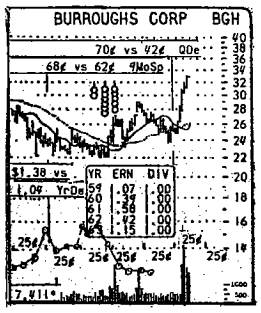
The greatest fiscal drama of the post-War era continues.

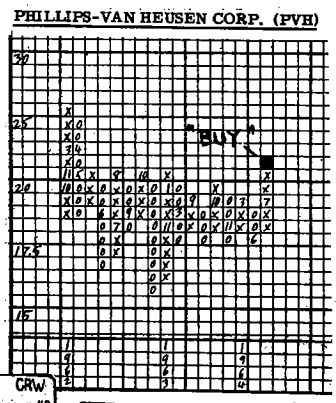
STOCKS: Strongest stock groups according to Chartcraft (Larchmont, N.Y.) are now Metal Fabricating, Food Chains, Vegetable Oils, Radio TV Broadcasters, Publishing, Textile Products, Apparel Manufacturers — in that order.

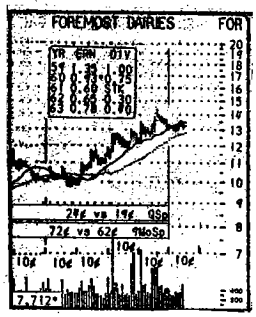
A number of stocks have been recommended for short-term trading in recent Letters, but I do not want to make the list to large. Burroughs recommended more than any other has been acting beautifully, and is hitting high after high. W.T. Grant is also doing very well, and both these issues have increased about 50% since my original recommendation. Crowell Collier

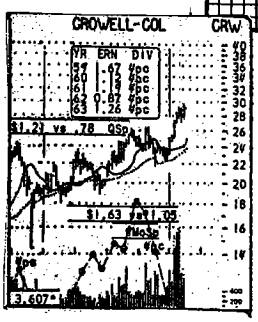


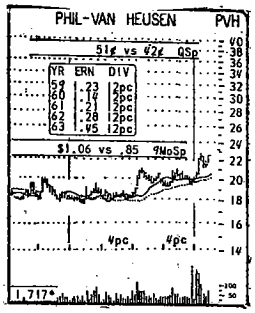



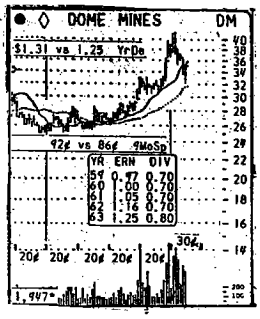



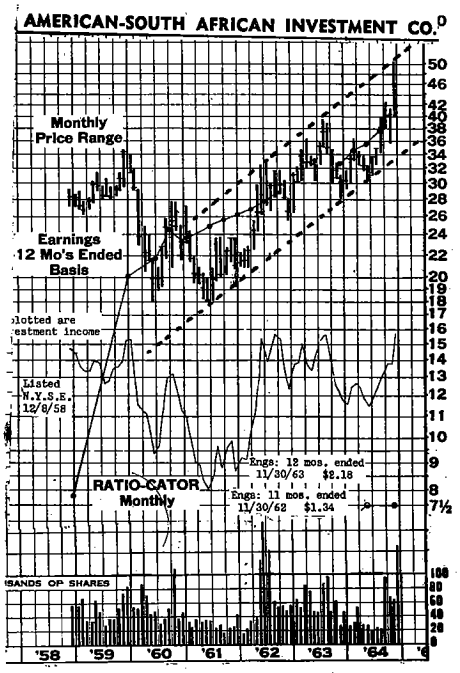




The apparel manufacturers are doing well, and one of the stocks which I particularly like in this group is Phillips-Van Heusen, makers of the famous Van Heusen shirt. At 22 the stock has just pushed out of a series of five tops as seen on the point & figure chart. This gives it a base for a potential rise to the mid-30's. Guardian Mutual Fund (one of the sharpest mutual funds in N.Y.) has recently taken a position in this one. I like PVH, I like its earnings trend, and I like the fact that nobody is talking about it — yet. This is an interesting stock, and it could do well even in a churning market. PVH is a new recommendation.





AMERICAN-SOUTH AFRICAN INVESTMENT CO.
Monthly Price Range
Earnings 12 Mo's Ended Basis
Listed N.Y.S.E. 12/8/58
RATIO-CATOR Monthly
Engs: 12 mos. ended 11/30/63 $2.18
Engs: 11 mos. ended 11/30/62 $1.34
'58 '59 '60 '61 '62 '63 '64

Because our Government forbids us to own gold bullion, the gold shares continue to be our only hedge against a potential monetary crisis and possible devaluation. Gold share ownership has been attacked from every quarter. Part of the 25% gold clause will soon be eliminated. But the former is "normal" and the latter is bullish for gold shares in that it definitely weakens the dollar in the eyes of the world (despite the bunk we hear from Washington). The chart of Dome is typical of the Canadian gold action. Dome has corrected back near its 200-day (dotted line) moving average, then rallied. I feel that DM and the rest of the golds are probably now beginning to form new bases for the next move. American-South African reflects the greater value and greater strength of the S African gold shares (which I still recommend as buys now). As of this writing, ASA is in the 45 area, near the upper part of the huge rising channel which has contained this stock since 1959. I see nothing wrong with ASA's action except perhaps that it went up too fast over the past few months. Interestingly, a short interest is now building up in some of the golds, perhaps the highest short interest in these stocks in 30 years. CRK has 15 thousand shorts listed against it, DM has 6. I consider this a big plus in the gold technical picture.

RECOMMENDED READING: This observer is an ex-World War II combat veteran and father of three children, one of whom is severely mentally retarded. If the "welfare state" offers anything, it seems to me that I will be near the head of the list for "the big payoff." I am nevertheless of the opinion that the government can only give me what it takes away from me and my fellow citizens (and I am not one of those cranks who believes that aged or incapacitated people should be allowed to starve in the streets). For those who would like to learn more about welfare trends, I recommend the following book by Wilhelm Ropke (he is one of the architects of the post-War German economy). Ropke's views on welfare and freedom are as intelligent as anything I have ever read on the subject, and the book clarified many of my own thoughts. Welfare, Freedom and Inflation by Ropke, Univ. of Alabama Press, University, Alabama, $2.95.

Small weekly charts courtesy of Quote Digest, 110 N. Lorraine, Wichita, Kansas. Chart of ASA courtesy of Security Research C Corp., 211 Congress, Boston, Mass. P & F chart of PHV courtesy of Chartcraft, Larchmont, N. Y.